



Treasury Trends

Bringing currency to the Arizona Taxpayer
David A. Petersen, State Treasurer

November 2005

THE OFFICIAL NEWSLETTER FOR ARIZONA LGIP PARTICIPANTS

This month's
character trait:

Initiative:

*The power or ability to
begin or to follow
through energetically
with a plan or task.*

*Know Whether or not
You are in a
Fiduciary
Relationship with
Investment
Providers.*

LGIP Performance

The Board of Investment was informed of the performance of the Local Government Investment Pool (LGIP), LGIP-Government, and LGIP-Core-Mix for the month to date and year to date period ending October 31, 2005 during its regular meeting on November 16, 2005.

Recent Pool performance is posted on the last page including a description of each Pool and a rolling twelve month performance table for the Pools offered by the Arizona State Treasurer's Office. Contacts and other information on the Pools can also be found on this condensed one page summary sheet for your convenience.

Investment Advice or Sales?

Ken Fisher, Deputy State Treasurer of Investments

Have you ever walked into an automobile dealership with the presumption that it is the salesperson's responsibility to know what the best transportation option for you is? More than likely the answer is no. We all know that there will be a bias to get us to buy what they are selling on their lot. We come in; tell them what we are looking for; and then they show us cars from their inventory that best match our descriptions.

Now, put yourself in the same scenario except that you are now dealing with an investment broker/dealer. After you fill out a questionnaire, the broker/dealer is going to show you bonds from their inventory or bonds they can underwrite. You then choose which bond is best for your investment program. The broker/dealer is acting under the "know your customer" rule. That is, they must know enough about your investment program to know what *not* to sell you. Everything else is fair game.

In the above scenario, the salesman is under no legal requirement to do what is best for your program. It is assumed that you have read and understand all of the disclosures you first received when you opened an account. If, for example, under State statutes you are allowed to buy US Government and Agency debt, which of the two do you think a salesperson will show you first:

1. A US Treasury security that they will trade with a very narrow bid/ask spread of \$100 per million sold; or
2. An Agency bond that may make around \$1,000 per million in underwriting fees from the Agencies.

Without any fiduciary responsibility, that is legal entrustment to those assets, the broker/dealer is legally free to offer you any investment as long as it is not inappropriate for your program. It is assumed that you, and not the broker/dealer, will ask for and then choose the investment that is best for your program. You are therefore responsible for those decisions and unless there is a legal fiduciary relationship, the one who sold you the bond is not.

There is a lot of grey area when it comes to investment advice. If you are looking for advice, then make sure that Advisor will not just say they are a fiduciary, but will be tied to that statement legally. Are they a registered investment advisor with the SEC and can they provide you with their form ADV? Will there be sufficient language in your account agreement to make them a fiduciary? Unless the answer is yes to that advice coming from a fiduciary, your financial goals may not necessarily line up with theirs.

At the End of November, There was less than 8bps Separating the 2 Year from the 10 Year US Treasury Note.

Ten Year Gains for First Time in Four Months

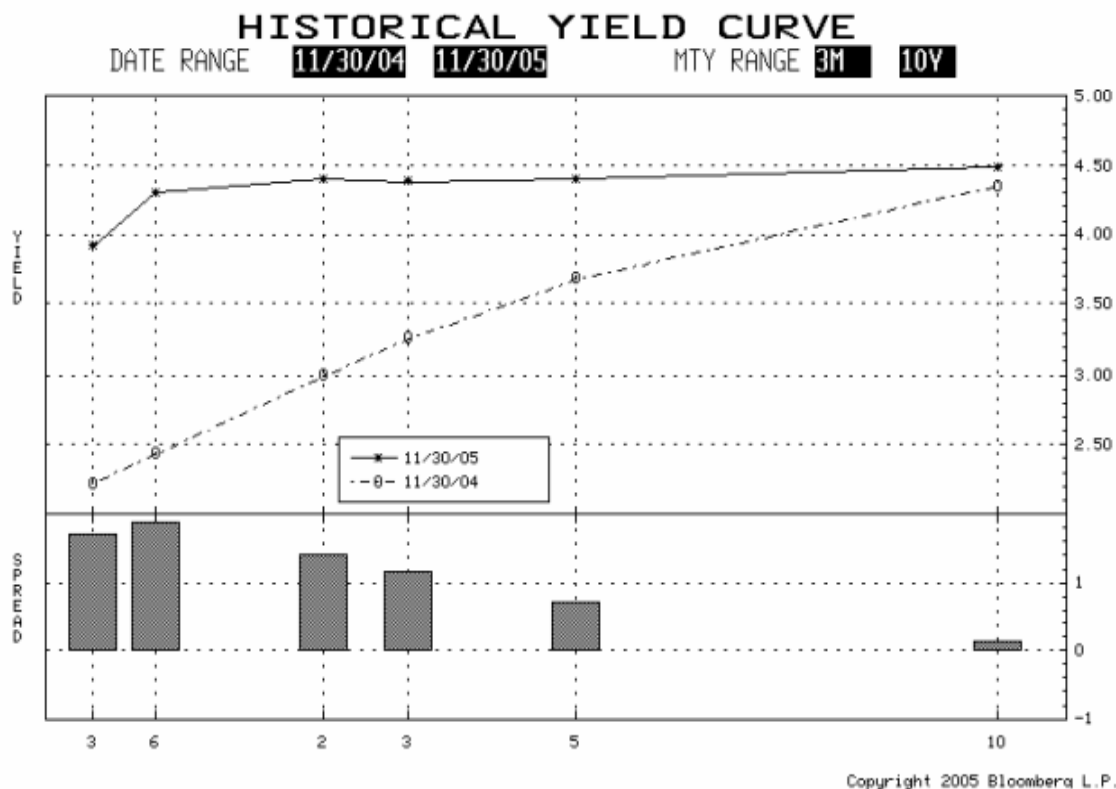
Ken Fisher, Deputy State Treasurer of Investments

If you look at the Yield Curve Perspective below, you can not help but notice the flattening of the US Treasury yield curve over the last year. Adding to this flattening was the gain in price of the US Treasury 10 year note in November, which in turn lowers the yield earned on an investment in that security. Additionally, crude oil prices also dropped during the month which eased many concerns some had that higher oil prices would lead to faster inflation. Without that risk of higher inflation, investors were tempted more to invest in the longer end of the yield curve since inflation should not then erode the future earnings they make on their longer term holdings.

As for the short end of the curve, the Federal Reserve is now poised to continue its path of raising the Fed Funds Target Rate at the next two meetings on December 13th and January 31st. In a recent survey done by Bloomberg, 71 economists had a median target of 4.75% for Fed Funds by the second quarter of 2006. For now, that mark certainly seems reasonable, but look for increases to taper off after we reach the 4.75% to 5.00% range by the end of next year.

Yield Curve Perspective (Source: Bloomberg LP)

Change in the 3 Month to 10 Year US Treasury Curve for One Year.



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We're on the Web!
www.aztreasury.gov

**LGIP: local & state government working together
to safeguard Arizona taxpayers' money.**

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Arizona State Treasurer's Office Local Government Investment Pools (LGIP) Fact Sheet on the Pools

OVERVIEW

LGIP (\$3.2 Billion as of 10/31/05)

Money market type fund designed to maximize your cash management program's efficiencies by providing a safe and reliable source of liquidity from the fund's portfolio of government and investment-grade domestic securities. Maximum weighted average maturity (WAM) is 240 days.

LGIP-Government (\$1.3 Billion as of 10/31/05)

Similar in style to the LGIP, but invests solely in securities that are backed by the full faith and credit of the US Government. Maximum WAM is 180 days.

LGIP-Core Mix (\$60.7 Million as of 10/31/05)

This fund invests in a longer term horizon than the LGIP cash management fund and adds the potential of total return from feasible price appreciation within the fund's portfolio of government and investment-grade domestic securities. Redemptions and Purchases are limited to the first business day of the month. Duration target is Merrill 1-5 US Domestic Master Index (not to exceed .75 years of index).

LGIP-Core-Government

Similar in style to LGIP-Core Mix, but invests solely in securities that are backed by the full faith and credit of the US Government. Duration target is Merrill 1-5 US Treasuries Index (not to exceed .75 years of index).

RECENT PERFORMANCE

LGIP			LGIP-Gov't		LGIP-Core		LGIP-Core-Gov't	
Month	Yield	WAM	Yield	WAM	Yield	NAV	Yield	NAV
Oct '05	3.53	66	3.37	121	3.91	1.000		
Sep '05	3.39	75	3.27	128	4.06	0.998		
Aug '05	3.22	79	3.22	130	3.65	1.000		
Jul '05	3.04	92	3.10	119	3.37	0.999		
Jun '05	2.90	84	2.72	152	3.55	1.001		
May '05	2.77	96	2.62	121	3.37	1.003		
Apr '05	2.63	99	2.37	104	2.84	1.000		
Mar '05	2.48	93	2.29	140	2.56	1.000		
Feb '05	2.47	100	1.92	125				
Jan '05	2.30	100	1.92	142				
Dec '04	2.21	146	1.80	79				
Nov '04	2.06	152	1.72	89				

Yields are net of fees

Initial Funding Mar-05 Currently Unfunded

ADVANTAGES

- Professionally managed by a team of educated, experienced former public investment officers and private sector portfolio managers and traders.
- Dedicated and separate Compliance, Accounting and Portfolio Management departments ensure our dedication to meeting the LGIPs' objectives.
- Bound by the Arizona Revised Statutes and the oversight of the Arizona Legislature.
- No contracts to negotiate. Accounts are opened with an executed governing body resolution.
- Pools are managed from the viewpoint of public entities for public entities.
- Multiple accounts within the Pools are available for your accounting needs.

IMPORTANT INFORMATION

Unless otherwise stated, investors are participating in a commingled investment pool in which they are conveyed a pro rata interest in the total value of all securities in that Pool. Investors share an apportioned amount of the Pool's income and expenses based on the average daily balances of participating accounts using the accrual basis of accounting. Investment products offered by the Arizona State Treasurer's Office are not backed, insured, or guaranteed by any bank, the FDIC, the State of Arizona, or any other Federal or State Government Agency. As with any investment, past history is not a guarantee of future performance and an investment may lose value.

Please refer to the most recent "Arizona State Treasury Investment Policy for Invested Monies" for further information and important disclosures in determining if an investment in one of the LGIPs is right for your organization. Contact us at 602-604-7800 or visit us at www.aztreasury.gov on the web.